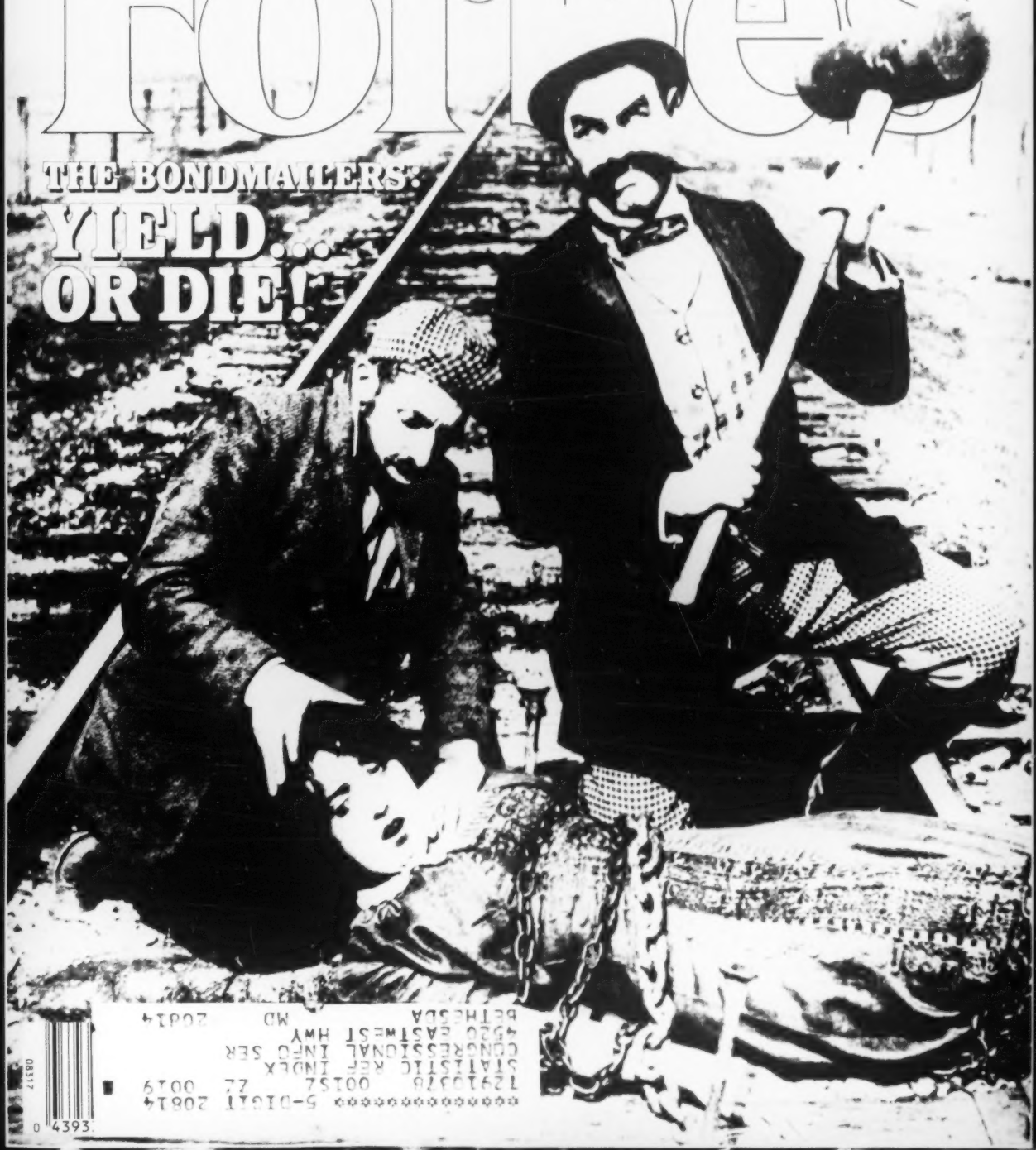
AUGUST 6, 1990 THREE DOLLARS SEVENTY-FIVE CENTS

Forbes

THE BONDMAILERS: YIELD... OR DIE!



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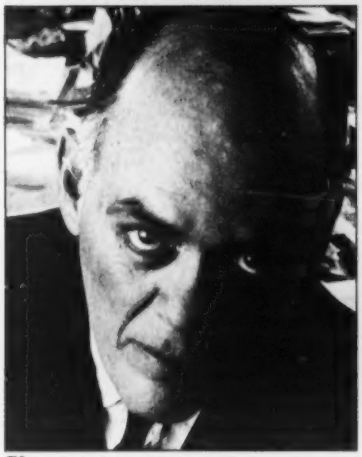

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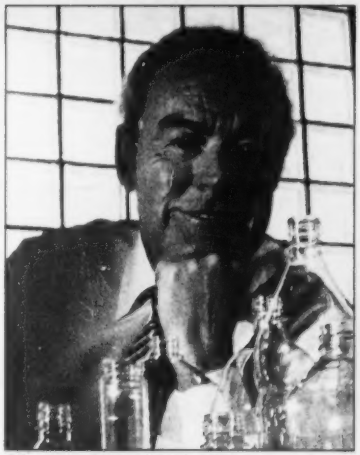

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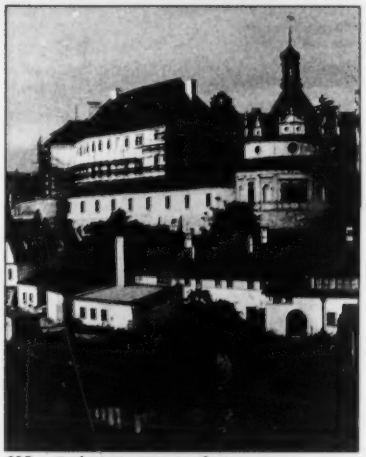

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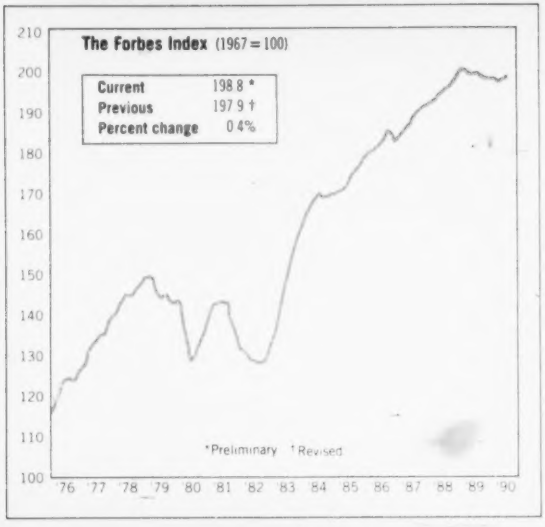
The Forbes Index



Buoyed by strong department store sales, retail volume recovered from a three-month slump to post a 0.5% gain in June. Unemployment fell in June for the third straight month, to 5.2% of the work force, but there may be trouble: The number of new unemployment claims rose 1.8%. After rising less than 0.1% in April, consumer installment credit increased 0.5% in May. The Forbes Index finished May with a 0.2% gain, the best monthly increase since January 1989. The preliminary June figure is up 0.4%, but only two components have been reported.

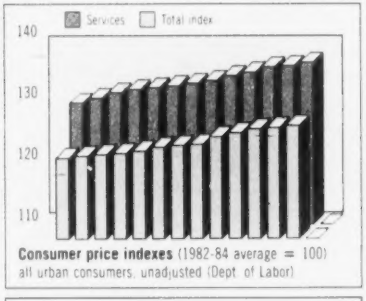
Other key rates	Source	Status
Prime rate	Chase Manhattan Bank	10.0%
Auto sales year to date vs. 1989[1]	Ward's Automotive	-3.7%
Index of leading indicators May vs. April	Dept of Commerce	0.8%
Trade balance last 12 months ending April 1990	Dept of Commerce	-$106 bil
Producer price index June vs. 1989[2]	Dept of Labor	3.1%
GNP 1st quarter vs. 4th—annualized growth	Dept of Commerce	1.9%
NBER Experimental Recession Index[3]	Natl Bureau of Economic Research	7.0%

[1]U.S.-based manufacturers, excludes imports, as of 7/10/90. [2]Finished goods. [3]May 1990

Index Components

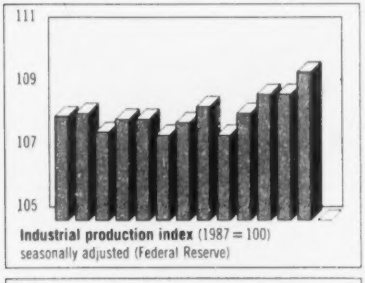
The Forbes Index is a measure of U.S. economic activity composed of 8 equally weighted elements: Total industrial production, new claims for unemployment compensation, the cost of services relative to all consumer prices, new housing starts, total retail sales, the level of new orders for durable goods compared with manufacturers' inventories, personal income, total consumer installment credit.

To measure these 8 elements, FORBES monitors 10 series of U.S. government data. The last 14 months' data for each series are presented below.



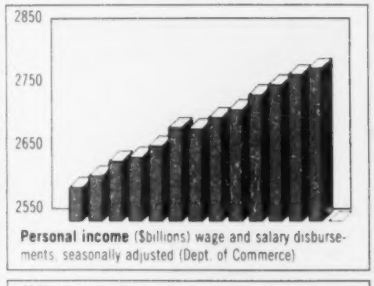
Consumer price indexes (1982-84 average = 100) all urban consumers, unadjusted (Dept. of Labor)

Manufacturers' new orders and inventories ($billions) seasonally adjusted (Dept. of Commerce)

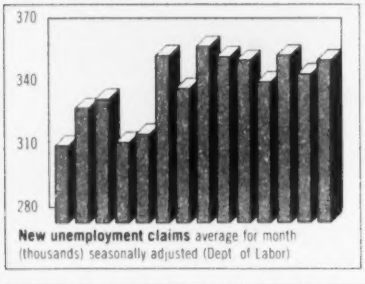


Industrial production index (1987 = 100) seasonally adjusted (Federal Reserve)

New housing starts (thousands) privately owned, unadjusted (Dept. of Commerce)



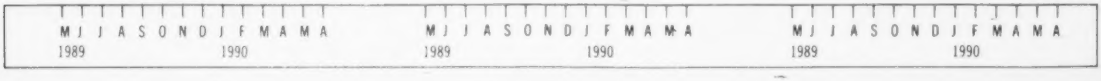
Personal income ($billions) wage and salary disbursements, seasonally adjusted (Dept. of Commerce)



New unemployment claims average for month (thousands) seasonally adjusted (Dept. of Labor)

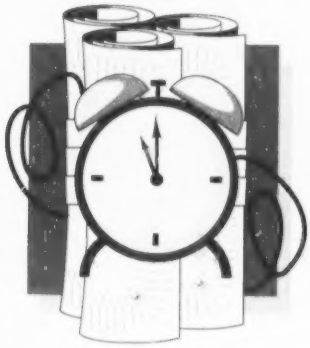
Retail sales ($billions) seasonally adjusted (Dept. of Commerce)

Consumer installment credit ($billions) total, seasonally adjusted (Federal Reserve)



Junk bombs are junk bonds with a built-in time bomb. Some are already exploding.

TICK, TICK, TICK



By Jason Zweig and David Stix

HOW DID SO MANY Wall Street firms justify their clients' issuing junk bonds in amounts and at interest rates that the clients' earnings could not cover? We're talking here not about run-of-the-mill junkers but of that special kind of junk bond that either paid no cash interest or paid it in some deferred form.

Isn't that close to fraud, selling bonds when you knew you weren't earning enough profits to pay the interest? No, because all the facts were in the prospectuses and because Wall Street is very good at rationalizing whatever fattens its pocketbook.

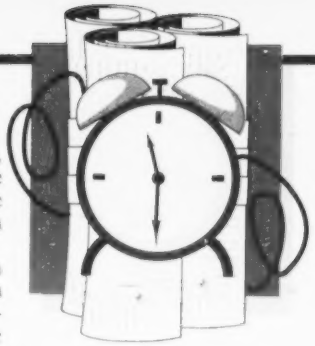
Listen to Joseph Bencivenga, the former head of high-yield research at Drexel Burnham Lambert, who now runs junk research at Salomon Brothers. He says that the aim of issuing bonds beyond a company's ability to service them was "to finance companies so they could grow into their capital structure." Is that a little like borrowing money for a trip to the racetrack in the hope of both paying the creditor and making the debtor rich? It is.

There are three main kinds of these "trigger" bonds:

Kaboom!

With the junk bond craze at its height a few years ago, scores of companies giddily issued "trigger" bonds. Before long, these bonds could detonate. At a predetermined date between now and 1996, the 50 companies listed here will likely be forced to come up with a load of cash to meet the bonds' sharply higher service costs. In some cases, cash interest payments could take up more than 100% of cash flow. Bondholders beware.

Company	Trigger event[1]	Issue size[2] ($mil)	Trigger date yr/mo/date	Current cash flow ($mil)[3,4]	—Annual cash interest ($mil)— current, on all debt[4]	increase as of trigger date	total as of trigger date[5]	Debt service coverage[6] %
Acadia Markets	PIK: 13.06	85.0	94/8/15	18.9	17.0	11.1	28.1	149
Adams-Russell	Split: 0/16¾	272.5	92/12/30	40.0	39.0	45.7	84.7	211
Adelphia Communications	Split: 0/16½	169.0	92/9/15	140.8	129.0	27.9	156.9	111
Air & Water Technologies	Split: 7½/13¾	84.0	91/4/15	49.1	31.3	5.3	36.6	75
Alco Health	PIK: 18½	42.7	94/10/31	57.6	55.7	7.9	63.6	110
American Standard	Split: 0/14½	545.9	93/6/30	443.1	219.9	77.8	297.7	67
Ann Taylor	Split: 0/14⅜	167.9	94/1/15	73.4	35.0	24.1	59.1	80
Burlington Holdings	Split: 0/16	271.7	93/10/1	319.9	160.0	43.5	260.8	81
Burlington Holdings	Split: 0/16	358.0	93/10/1	319.9	160.0	57.3	260.8	81
Cablevision Systems	Reset: 12¼/14	200.0	91/5/15	230.0	185.0	3.5	188.5	82



There are payment-in-kind bonds, which pay interest in the form of more bonds in the early years and then—in the sweet bye-and-bye—switch to large cash payments.

There are split-coupon bonds, which generally pay little or no interest for a few years and then promise—promise—to pay extremely high interest in the bond's later years.

There are resets, which pay relatively low interest rates in the early years and then are reset on a predetermined date, usually to a substantially higher rate, depending on market conditions.

Did it make sense to buy bonds issued on this basis? Recalls Wayne Josephson, a high-yield analyst at Fitch Investors Service: "The herd instinct took over the whole investment banking community once again, and everyone seemed to buy the same line." Those whom the gods would destroy they first make mad.

In December 1988, at the tail end of the junk-issuing frenzy, the average yield on junk with cash coupons was around 12.90%, versus 14.85% for junk with deferred coupons—a yield spread of only 190 basis points. As of last month, the yield on cash-paying junk had crept up to 15.25%, but deferred paper was trading at a vertiginous yield of 19.10%.

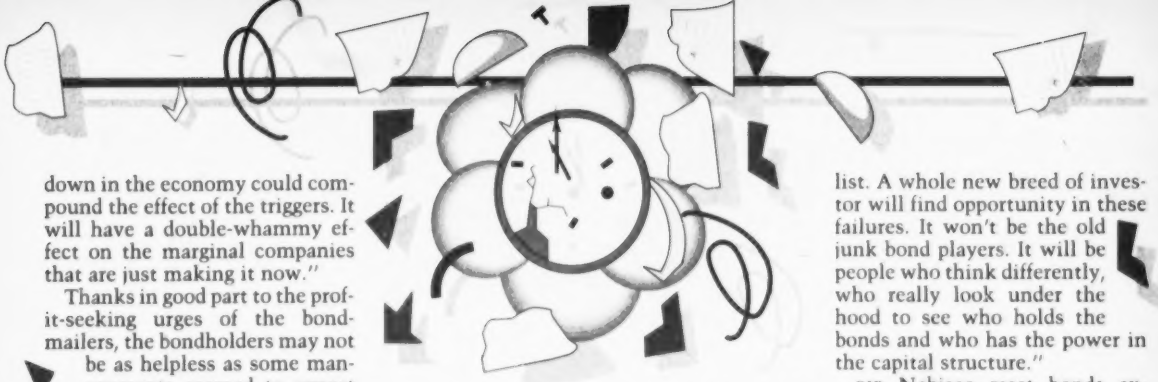
FORBES has identified roughly 200 companies that issued trigger bonds in the late 1980s. That's some $40 billion of junk debt. In 1991 and 1993, two peak years, some $10 billion worth of bonds must begin paying cash interest or be reset to higher rates.

Warns Josephson of Fitch Investors Service, "Any slow-

Company	Trigger event[1]	Issue size[2] ($mil)	Trigger date yr/mo/date	Current cash flow ($mil)[3,4]	—Annual cash interest ($mil)— current, on all debt[4]	increase as of trigger date	total as of trigger date[5]	Debt service coverage[6] %
Calmar Spraying Systems	Split: 0/14	150.0	92/2/15	38.6	15.0	21.0	36.0	93
Charter Medical	Split: 0/13	240.0	91/8/16	281.6	127.0	31.2	158.2	56
Charter Medical	PIK: 15.85	243.3	95/8/15	281.6	127.0	38.6	196.8	70
Cherokee Group	Reset: 9/17½	117.5	92/5/1	34.4	17.5	10.0	27.5	80
Club Car	Split: 10/14½	76.0	92/4/1	15.0	9.0	3.4	12.4	83
Colt Holdings	Split: 0/14⅜	920.0	93/7/15	320.5	135.0	135.7	270.7	85
Cullum Co	Split: 0/16	260.0	93/12/1	75.2	30.4	41.6	72.0	94
Dr Pepper/Seven-Up	Split: 0/15½	541.2	93/4/1	199.1	76.2	83.9	160.1	80
Duracell Holdings	Split: 0/13⅛	670.0	93/9/15	287.0	147.0	87.9	234.9	82
Duff & Phelps Funding	PIK: 15	75.0	92/3/1	14.3	5.0	11.2	16.3	113
Eckerd Holdings	Split: 0/13	345.2	91/5/1	230.5	115.7	44.9	160.6	70
Edgcomb Metals	Split: 9/15	138.5	94/8/15	28.6	19.8	8.3	28.1	98
Envirodyne Industries	Split: 0/14½	250.0	94/8/1	106.8	80.0	36.3	116.3	108
EPIC Healthcare	PIK: 11	50.0	95/9/30	93.0	50.0	5.5	55.5	60
Fort Howard	PIK: 14⅝	446.5	94/11/1	458.0	329.0	182.1	511.1	112
Fort Howard	Split: 0/14⅛	827.0	94/11/1	458.0	329.0	182.1	511.1	112
Gaylord Container	Split: 0/16½	125.8	92/5/1	121.0	65.0	20.8	85.8	70
Harcourt Brace Jovanovich	PIK: 14¾	357.0	92/9/15	102.3	247.5	53.0	353.3	345
Harcourt Brace Jovanovich	Split: 0/14¾	358.0	92/9/15	102.3	247.5	52.8	353.3	345
Healthtrust	Split: 0/16½	365.0	91/12/1	274.7	123.3	60.2	196.3	72
Healthtrust	Split: 0/11.6	110.0	91/12/1	274.7	123.3	12.8	196.3	72
Hospital Corp of America	Split: 0/15¾	444.0	91/8/1	903.0	475.0	69.9	545.0	60
Joy Technologies	Reset: 13/15½	120.0	91/11/15	51.1	50.4	3	53.4	104
JPS Textile Group	Split: 0/18¾	160.0	92/6/1	76.9	69.2	30	99.2	129
Kroger	Split: 0/15½	1,375.3	93/10/15	895.8	460.0	213.1	673.0	75

[1]For splits and resets, the number before the slash is the current interest rate. On splits, the number after the slash is rate after trigger date; on resets the number after the slash is the maximum possible interest rate. Maximum rate is used in all subsequent calculations. [2]Amount currently outstanding; many will be larger by trigger date. [3]Earnings before tax, interest, dividends, depreciation and amortization. [4]For most recent 12-month period available. [5]Projected, by adding increase in annual interest payments after trigger date to current annual cash interest payments. [6]Percent of cash flow needed to cover projected annual interest after trigger date. [7]Assuming Viacom reset takes place at 11½%. NM: Not meaningful.

Sources: Donaldson, Lufkin & Jenrette, Fitch Investors Service, IDD Information Services, Indepth Data, Salomon Brothers, Securities Data Corp.



down in the economy could compound the effect of the triggers. It will have a double-whammy effect on the marginal companies that are just making it now."

Thanks in good part to the profit-seeking urges of the bondmailers, the bondholders may not be as helpless as some managements seemed to expect *(see story, p. 74)*. Gregory Smith, president of Indepth Data, an Oklahoma City-based junk bond research firm, helped compile the table accompanying this story. Says Smith: "This is both a watch list and an opportunity list. A whole new breed of investor will find opportunity in these failures. It won't be the old junk bond players. It will be people who think differently, who really look under the hood to see who holds the bonds and who has the power in the capital structure."

RJR Nabisco reset bonds exploded and bondholders screamed. The equity owners, Kohlberg Kravis Roberts, had to put in a lot of additional capital, providing extra protection. The bonds' prices recovered smartly. In danger there is opportunity. ■

Kaboom!

Company	Trigger event[1]	Issue size[2] ($mil)	Trigger date yr/mo/date	Current cash flow ($mil)[3,4]	—Annual cash interest ($mil)— current, on all debt[4]	increase as of trigger date	total as of trigger date[5]	Debt service coverage[6] %
Macy Merger	Split: 0/16	881.1	93/7/15	730.9	589.8	141.0	739.9	101
Malrite Communications	Split: 0/15⅛	167.0	94/2/15	18.0	12.0	25.5	37.5	208
Maryland Cable	Split: 0/15⅜	162.4	93/11/15	15.7	9.6	25.0	34.6	220
Morse Shoe	Split: 8¼/16	221.0	91/3/15	47.9	32.7	17.1	49.8	104
MS/Essex Holdings	Split: 0/16	342.0	95/11/15	110.7	35.9	54.7	90.6	82
Musicland Stores	Split: 12/14¾	53.5	91/9/30	85.1	42.7	1.5	44.2	52
National Gypsum	Split: 0/15½	572.7	91/7/1	126.1	77.5	88.8	166.3	132
Owens-Illinois	Split: 0/15	400.0	93/6/1	719.5	418.5	60.0	576.9	80
Owens-Illinois	PIK: 14½	678.6	93/6/1	719.5	418.5	98.4	576.9	80
PA Holdings	Reset: 12¾/15	235.0	90/8/15	157.5	121.0	5.3	126.3	80
PA Holdings	PIK: 13¼	120.0	93/8/15	157.5	121.0	15.9	142.2	90
Panhandle Eastern	Reset: 11⅝/14⅛	300.0	91/8/1	694.4	448.8	7.5	456.3	66
Playtex Apparel	Split: 9/14	182.0	94/4/1	79.3	40.0	9.1	49.1	62
Reliance Electric	Split: 0/14	393.0	92/4/1	231.0	50.0	55.0	105.0	45
SSC Holdings	Reset: 12½/15	125.0	91/7/15	241.8	132.5	3.1	135.6	56
Supermarkets General	Split: 0/13⅛	182.6	92/10/5	326.5	180.0	24.0	204.0	62
Supermarkets General	PIK: 12⅝	320.0	92/12/15	326.5	180.4	40.4	244.8	75
Tonka	PIK: 17¼	120.1	92/12/1	153.0	77.0	20.7	97.7	64
Triad Systems	Reset: 14/16½	80.0	92/8/1	29.1	11.0	2.0	13.0	45
TW Services	Split: 0/17	712.1	94/11/1	396.3	174.5	121.1	295.6	75
TWA	PIK: 12	391.3	90/9/30	11.4	366.2	47.0	413.2	NM
TWA	PIK: 12	250.7	90/10/24	11.4	366.2	30.1	443.4	NM
USG	PIK: 16	337.7	93/7/16	416.0	251.0	54.0	305.0	73
Viacom	Split: 0/14¾	399.5	91/6/15	341.9	169.1	58.9	228.0	67
Viacom	Reset: 11½/no maximum	193.0	91/7/15	341.9	169.1	—	228.0	67[7]
Viacom	PIK: 15½	340.3	93/6/30	341.9	169.1	52.8	280.8	82

[1]For splits and resets, the number before the slash is the current interest rate. On splits, the number after the slash is rate after trigger date; on resets the number after the slash is the maximum possible interest rate. Maximum rate is used in all subsequent calculations. [2]Amount currently outstanding; many will be larger by trigger date. [3]Earnings before tax, interest, dividends, depreciation and amortization. [4]For most recent 12-month period available. [5]Projected, by adding increase in annual interest payments after trigger date to current annual cash interest payments. [6]Percent of cash flow needed to cover projected annual interest after trigger date. [7]Assuming Viacom reset takes place at 11½%. NM: Not meaningful.

Sources: Donaldson, Lufkin & Jenrette; Fitch Investors Service; IDD Information Services; Indepth Data; Salomon Brothers; Securities Data Corp.

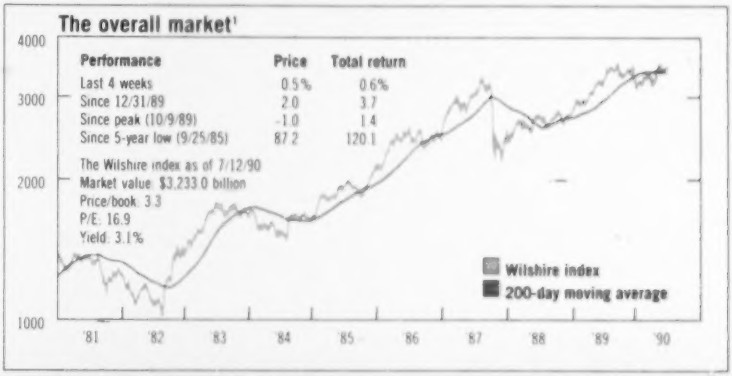
The Forbes Wall Street Review

By Eric S. Hardy

"Stock prices should go higher not because earnings are great but because the market thrives on lower interest rates," says John D. Connolly, chief investment strategist at Dean Witter. Connolly believes interest rates will be lowered by a higher U.S. savings rate and reduced credit demand. As a result, he expects the yield of the S&P 500, currently at 3.4%, to soon decline to around 3%, putting the Dow at about 3300.

Although the housing market is showing no signs of recovery, Robert Curran, who follows the industry for Merrill Lynch, is recommending some stocks that are peripherally involved in the housing business. He likes Lowe's (a retailer that sells home-building supplies) and PPG Industries, which makes glass for both the automotive and housing markets.

Utility and natural gas stocks are often bought by risk-averse investors seeking nice yields and relatively steady prices. Nevertheless, two of the most volatile stocks during the past two weeks were in these industries. Contel (a telephone utility) shot up 39% when it agreed to merge with GTE. Natural gas distributor Panhandle Eastern dropped 23% because of speculation that it would "review" its dividend policy at the board meeting scheduled for late July. The stock currently has a double-digit yield, but there's a good chance the $2 annual payout will be reduced.



The Best Performing Stocks

Company	Price	2-week change	P/E	Avg vol (thou)[2]	Rel vol[3]
Contel	35⅛	39%	21	7,770	2.5
General Instrument	46⅛	29	15	9,128	6.7
TJX Cos	16¼	25	NM	2,602	0.8
McDonnell Douglas	43⅛	22	33	2,372	2.2
Acuson	46⅛	20	27	765	1.3

The Worst Performing Stocks

Company	Price	2-week change	P/E	Avg vol (thou)[2]	Rel vol[3]
Computer Assoc Intl	10¼	-34%	12	5,815	1.1
Panhandle Eastern	18⅛	-23	21	9,874	2.4
Mentor Graphics	17	-23	14	11,571	2.2
TCBY Enterprises	14⅛	-23	13	5,248	1.8
Signet Banking	18¼	-19	4	1,224	3.0

Closeup on the Market

Index or investment	Price	2-week change
Wilshire index 6,000 stocks, capitalization weighted	3,488.21	2.1%
Wilshire index 6,000 stocks, equal weighted	22.02	1.0
Dow Jones industrials 30 stocks, divisor-adjusted price average	2,969.80	3.2
S&P 500 Capitalization weighted cross section, major stocks	365.44	2.2
NYSE Capitalization weighted, all listed common stocks	199.32	2.1
Amex Capitalization weighted total return: stocks, warrants	362.23	1.0
Nasdaq Capitalization weighted, all issues except warrants	467.17	1.5
Amex international market index Capitalization weighted, 50 largest ADRs	330.39	3.5

Index or investment	Price or rate	2-week change
Europe, Australia, New Zealand and Far East[4] (EAFE) a dollar denominated capitalization weighted index	930.40	2.3%
Institutional[5] Approximately 200 stocks with high institutional ownership	119.59	1.7
Individual[5] Approximately 200 stocks with low institutional ownership	106.19	0.5
Russell 2000 index 2000 stocks with small market values, capitalization weighted	169.43	0.6
Gold[6] (composite quote of 6 major dealers)	$358.30	1.0
Yen[6] (per $U.S.)	147.50	-3.7
Commodity index[6] (CRB futures index, 1967 = 100)	233.55	-1.0
Oil[6] (W Texas Intermediate)	$18.45	7.6
T bills[6] (90 days)	7.65%	-8 basis points[7]
Broker loan rate[6]	9.25%	unchanged

Note: All data for periods ending 7/12/90. Wilshire index reflects price performance. It differs slightly from market value of outstanding stocks because of retirements of equity since index was created. Stocks listed above have market capitalizations of $500 million or more. [1]Capitalization weighted, prepared by Wilshire Associates, Santa Monica, Calif. [2]Average daily volume over a 2-week period. [3]Average daily volume over the last 2 weeks, divided by the average daily volume over the preceding 3 months. [4]Morgan Stanley Capital International Perspective. [5]For period ending 7/13/90. A. Arbel, Cornell University, using Ford Database from Ford Investor Services. [6]Knight-Ridder Financial Information. [7]A basis point is equal to one-hundredth of a percentage point. NM: Not meaningful.

New Issues Review

By Robert Balancia

The biggest[1]

Company/business	Exchange	Offer date	Offer price	Recent price	Offering ($mil)	Lead underwriter	Performance to date absolute	Performance to date rel to mkt[2]
Transatlantic Holdings/fire, marine ins	N	6/15/90	27	27 ¾	$157	Goldman Sachs	3%	104%
Safeway/supermarkets	N	4/25/90	11¼	14 ⅜	90	Goldman Sachs	27	119
Fingerhut/mail order catalog	N	4/25/90	16½	21 ¾	83	Smith Barney	32	122
Pool Energy Svcs/oilfield svcs	O	4/17/90	10¼	12 ⅛	82	Shearson Lehman	21	113
RMI Titanium/titanium prods	N	4/12/90	12½	11 ¼	75	First Boston	–10	84
Chiles Offshore/oilfield svcs	A	5/24/90	14½	11 ⅛	73	Bear Stearns	–21	79
Mid-Am Waste Sys/waste mgmt svcs	O	5/18/90	24	38 ⅜	72	Alex Brown & Sons	61	159
Horsehead Res Develop/metals	O	6/29/90	14½	18	47	Kidder Peabody	24	124
Granite Construction/construction	O	4/20/90	17	23 ¾	43	Smith Barney	40	131
Mr Coffee/mfr coffeemakers	O	5/31/90	10	14 ⅛	40	Alex Brown & Sons	47	148

Performance Update

In the past 12 months, underwriters of new issues raised more money, $472 million, for oil and gas explorers than for any other industry. Although it is a far cry from the frenzied underwriting of energy stocks during the late 1970s and early 1980s, it does signal a renewed interest in this sector. During the past quarter two of the largest new issues were oilfield service firms. The largest is Pool Energy Services of Houston, an $82 million deal underwritten by Shearson Lehman.

Waste disposal is another hot area. Two stocks in this sector, Mid-American Waste Systems and Sanifill, were among the best-performing new issues of the past quarter. Both were underwritten by Alex. Brown & Sons.

Safeway Stores was the second-largest IPO during the quarter. It had been taken private by Kohlberg Kravis Roberts in 1986. At the time of its LBO Safeway had revenues of $20.3 billion and 2,284 stores. Safeway sold assets to pay for its buyout. It now has 1,117 stores and revenues of $14.3 billion.

Newark N.J.-based Securities Data Co., the firm that provided the information in the accompanying tables, reports that the amount of money raised in the second quarter (excluding small offerings; see footnote) increased from $1 billion in 1989 to $1.6 billion in 1990.

The best[1]

Company/business	Offer price	Offering ($mil)	Lead underwriter	Performance to date absolute	Performance to date rel to mkt[2]
Sanifill/waste mgmt svcs	9½	$19	Alex Brown & Sons	113%	199%
Sullivan Dental Prods/dental prods	10	10	Dain Bosworth	88	178
Fleer/confection goods	15	26	Smith Barney	70	172
Mid-Am Waste/waste mgmt svcs	24	72	Alex Brown & Sons	61	159
RasterOps/imaging prods	12	22	Robertson Stephens	58	152

The worst[1]

Company/business	Offer price	Offering ($mil)	Lead underwriter	Performance to date absolute	Performance to date rel to mkt[2]
Gensia Pharm/pharmaceuticals	11	$31	Alex Brown & Sons	–25%	77%
Immune Response/med research	7	15	Dillon Read	–23	72
Curragh Resources/mining	10	25	Morgan Stanley	–23	78
Chiles Offshore/oilfield svcs	14½	73	Bear Stearns	–22	79
Wahlco Environ Sys/filter prods	13	23	Prudential Bache	–12	82

The most active investment bankers[1]

Underwriter	Total offerings	Total raised ($mil)
Goldman Sachs	13	$1,237
Alex Brown & Sons	23	580
First Boston	6	509
Lehman Brothers	6	444
Morgan Stanley	8	362

Industries going public[1]

Industry	Total offerings	Total raised ($mil)
Oil & gas exploration	5	$472
Magazine publishing	1	420
Typewriters	1	252
Computer systems	7	224
Audio records	1	224

Notes: Initial public offerings of common equities with offer date of 4/1/90 to 6/30/90, offering price of $2.50 or more and offering value of $5 million or more. Closed-end funds, limited partnerships, and ADS (American Depositary Shares) of corporations already traded in foreign countries are excluded, as are REITs and spinoffs. [1]Last quarter. [2]The ending value of $100 invested in the stock, divided by the ending value of $1 invested in the market. [3]Latest 12 months. Source: Securities Data Co.